

H-3107-1 - CONTINUATION, EXTENSION, OR RENEWAL OF LEASES

KeywordsI. Extension by Drilling on Federal Lands

A. General. Lease extension by drilling is only authorized for actual drilling operations that were commenced prior to and are being diligently conducted over the expiration date of the primary term of the lease. Such an extension is not available for drilling over the end of an extended term of any lease issued on or after September 2, 1960, including any extended term of a lease by reason of previous drilling extension, segregation of a lease committed in part to a unit, elimination from a unit or CA, and similar extensions. An approved suspension of operations and/or production for any period beginning before the end of the primary lease term shall serve to extend the primary term by a period equal to the period of the suspension. (See Manual Section 3103 and Handbook 3103-1.) A lease may still be eligible for a drilling extension if drilling operations are conducted over the end of the primary term even though this lease has previously been granted an extension for any other reason. However, a lease in this situation would be eligible for a drilling extension from the date of the end of the primary term, not from the date of any extended term. (See Solicitor's Opinion of May 17, 1984, at Appendix 1.) For leases issued prior to September 2, 1960, diligent drilling extensions may be earned at the end of extended terms, provided the lease has not been previously extended by production. (See Ashland Oil, Inc., et al., 79 I.D. 532 (1972).)

EXTENSION BY
DRILLING

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Keywords

B. Determination of Actual Drilling Operations. The following guidance is to be used in making the determination whether the activities of an operator constitute actual diligent drilling operations on a lease:

DETERMINATION
OF ACTUAL
DRILLING
OPERATIONS

1. Serious Effort. An essential characteristic of actual drilling operations is when such operations are conducted in a manner as to be a continuous effort (not necessarily the best effort, but a sincere effort) that an operator seriously looking for oil and gas could be expected to make in that particular area, given the existing knowledge of geologic and other factors normally considered when drilling for oil and gas. The well must be designed to test at least one potentially productive oil and gas formation, given the existing knowledge of geologic factors for the particular area. However, a lessee has the right under the terms of the lease to drill at any location on the leased lands that spacing and environmental factors in the area permit and to drill (or deepen) to any formation selected in search of oil or gas. There is no obligation on the part of the authorized officer (AO) to gather, study, or evaluate the existing knowledge of geological and other factors, or to inform the operator of the Bureau's conclusions at the time approval is given to drill (or rework). Accordingly, the approval of the Application for Permit to Drill (APD) does not indicate any determination that the proposed formation to be tested will qualify the lease for an extension by drilling. However, in cases where the AO is aware that the proposed formation will not qualify as a potentially productive formation for purposes of a drilling extension, the AO should so advise the applicant. (See Standard Oil Company of Texas, A-30137, A-30221, 71 I.D. 257 (1964).

SERIOUS EFFORT
TO DRILL

Drilling operations lacking the above characteristic cannot be deemed actual drilling operations. Actual drilling operations do not include such preparatory or preliminary work as grading roads and well sites, drilling the "rat" hole or moving equipment onto the lease. General guidelines may be set, but the official interpreting the facts in each case must use judgment within those guidelines. (See Solicitor's Opinion, M-36657, July 17, 1963, at Appendix 2, and Thelma M. Holbrook et al., A-30940, 75 I.D. 329 (1968).

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Keywords2. Verification of Drilling Operations.

Drilling operations do not have to be inspected precisely on the expiration date of the lease. Drilling operations are to be inspected prior to the lease expiration date to ensure that actual drilling has commenced. However, a signed statement from the operator, drilling contractor, or operator's onsite representative, if the drilling contractor has not personally witnessed the operations, certifying that drilling operations were commenced prior to the lease expiration date, along with supporting evidence documenting what operations took place on the last day of the primary term, can be accepted if it is not practical for the FO operations personnel to timely inspect the operations.

VERIFICATION
OF DRILLING
OPERATIONS

3. Justifiable Cause. Approved cessation of operations due to severe weather or other justifiable cause can be counted as diligent drilling for lease extension if such drilling operations were commenced before the lease expiration date and are timely resumed (as determined by the AO) and continued diligently to completion.

JUSTIFIABLE
CAUSE FOR
CESSATION OF
DRILLING
OPERATIONS

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Keywords

4. Completion Date, Testing, End of Drilling Operations. In the absence of specific approval by the AO to delay further work, if no physical or mechanical changes have occurred in the well for over 60 days, the well is to be considered completed, suspended, or temporarily abandoned, and diligent operations shall be considered as having ceased on the date that last operations were conducted on the well. When drilling operations are in progress on the last day of a lease's primary term (a lease expires at midnight on a specific date), the drilling operations must be in progress on that date and must continue thereafter until a potential target formation is penetrated. Generally, a well is considered completed after the first zone that establishes production is perforated and treated, or after such other completion methods as are standard in a field are performed and an initial production test is taken. Subsequent perforating, fracture acidizing, and testing are normally considered remedial or workover operations and are not considered as diligent drilling for purposes of lease extension. If drilling operations stopped a few hours before the moment of lease expiration, e.g., at 5:00 p.m. on May 31, 1994, and this conclusion time was not the end of the initial production test, with plugging of the hole occurring prior to the end of the 60-day period, the drilling operations on the last day of the lease's primary term would not serve to extend the lease. Extended periods of testing 60 days beyond the initial production test normally shall not qualify as diligent drilling operations. However, in a few cases, the formation depths and geologic characteristics of the area may warrant testing in excess of 60 days. Such extended periods of testing may qualify as diligent drilling operations for lease extension purposes if approved in advance by the AO. In cases of either a dry hole or nonproductive well where no production test is performed, the well is considered completed after 60 days have elapsed in which no drilling, testing, completing, or equipping operations have occurred, effective the date that such operations were last conducted on the well. If the well is plugged prior to the end of the 60-day period, the effective completion date is the date operations were last conducted on the well.

COMPLETION,
TESTING, AND
END OF
DRILLING
OPERATIONS

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Keywords

5. Down-hole Equipping. The regulations at 43 CFR 3100.0-5(g) state that actual drilling operations include "the testing, completing, or equipping of such well for production." The term equipping is interpreted to mean the equipping of the hole (casing, tubing, packers, pumps, etc.) so that it is capable of producing hydrocarbons to the surface.

DOWN-HOLE
EQUIPPING

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Keywords

C. Guidance for Drilling a New Hole. In addition to the guidance under Section I.B, above, the use of a small rig to spud and set conductor pipe or surface casing prior to or across the lease expiration date can be considered as diligent drilling operations if the casing program and hole size are appropriate for the well objective, the setting of conductor pipe or surface casing is necessary for operations in the field or area, and such operations have been approved in the APD. However, a large or full sized rig must be moved in later (within 30 days, unless otherwise approved by the AO) and must continue diligent drilling operations on the hole until a potential oil or gas formation is reached. Delays of more than 30 days must be due to reasons beyond the operator's control and must be justified to, and approved by, the AO. Preliminary activities such as grading of access roads and the drill site or moving equipment onto the lease commenced prior to the end of the primary term shall not by itself qualify as actual diligent drilling operations. (See Burton W. Hancock, 31 IBLA 18 (1977) and Michigan Oil Company, A-29828, 71 I.D. 263 (1964).)

GUIDANCE FOR
DRILLING
NEW HOLE

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KeywordsGUIDANCE FOR
DRILLING IN
PREVIOUSLY
DRILLED WELL

D. Guidance for Drilling in a Previously Drilled Well. In addition to guidance provided under Section I.B, above, operations in an old well can only be considered as actual drilling operations for purposes of lease extension if a drilling rig is on the hole and drilling the new hole over the lease expiration date. Operations in an old hole that are designed to attempt completion in a shallower zone, or that do not lead to deepening of the original hole, cannot be considered as actual drilling operations. (See Morton Oil Company, A-27392, 63 I.D. 392 (1956).) Likewise, plugging operations to abandon a previously drilled well do not constitute diligent drilling operations. The hole that is being drilled over the lease expiration date must be continued with diligence until at least one new and deeper potential oil or gas formation is penetrated. However, when continued operations in the old hole are impossible due to lost tools or other valid reasons, the skidding of the rig to a new location, in the same spacing unit, on the lease and the subsequent drilling of a new well to the objective zone or formation may be considered as diligent operations, if the new hole is diligently drilled to a potential oil or gas zone. The commencement of the subsequent drilling must normally be within 30 days of the discontinuance of operations in the old hole. Under this circumstance, the additional guidance under Section I.C, above, applies.

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E. Diligent Drilling in Communitization and Unit Agreements. Diligent drilling of a well on a committed tract within a federally approved CA or unit shall be considered as diligent drilling for each and every committed Federal lease. However, to be considered diligent operations for such agreements and the leases committed thereto, the well must be diligently drilled to the formation covered by the CA or to a potentially productive formation covered by the unit agreement. If the well has penetrated a potential oil or gas formation that is not the communitized formation or the formation specified in the unit agreement, the lease drilling extension shall apply to the lease where the well is actually located, but not to any other leases committed to the CA or unit. Final determination of lease extension by drilling is not to be made until the public interest requirement for the CA or unit has been met. However, a preliminary report is to be submitted to the SO fluid lease adjudication as soon as possible, so it becomes aware of possible lease extensions.

DILIGENT
DRILLING IN
CA OR UNIT
AGREEMENT

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Keywords

F. Reports to SO Lease Adjudication. Where actual drilling operations are in progress over the expiration date of any lease, the AO must submit either a preliminary or final report to SO fluid lease adjudication. If it appears the drilling operation is one that a person seriously looking for oil or gas in the area could be expected to make and operations have reached a legitimate depth, i.e., a horizon that is potentially productive, a final report of diligent drilling must be made (see Illustration 1).

REPORTS TO
SO FLUID
LEASE
ADJUDICATION

If there is any question in the matter, or if a well within a communitized or unitized area has not yet reached a communitized or unitized formation or depth, the AO's report should be preliminary and indicate that operations have commenced that may result in a lease extension (see Illustration 2). After drilling operations have been completed, a final report is to be made to the SO fluid lease adjudication. Where such drilling operations cause a suspension of operations and/or production to be lifted, the report must indicate the precise date the drilling commenced or resumed and the effect on the suspension. Reports indicating that extension of a lease is warranted in accordance with 43 CFR 3107.1 need only state that actual drilling operations were conducted diligently over the expiration date of the lease. However, if a determination is made that operations were not sufficiently diligent to qualify for lease extension, the report must contain sufficient details to justify this conclusion (see Illustration 3). This report is to include the following items:

PRELIMINARY/
FINAL REPORT
OF DILIGENT
DRILLING

1. The objective formation.
2. The date drilling commenced, and the total depth and casing run at the time of recommendation.
3. Statement that formations penetrated at that depth are not considered to be potentially productive of oil and/or gas.
4. Any other appropriate information that shows that the operation does not qualify for a drilling extension under 43 CFR 3107.1.

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Keywords

G. Rental Requirements. The annual rental payment must be paid on or before the lease anniversary date for any lease anticipating an extension. (See 43 CFR 3107.1 and Oil Resources Inc., 28 IBLA 394 (1977).) Lessees should be urged to ensure that such rental payments are timely made when drilling operations to extend a lease are planned, since the lease will automatically terminate by operation of law in accordance with 30 U.S.C. 188(b) in the absence of such timely annual rental payment. While the possibility of lease reinstatement in such instances exists, the cost to the lessee shall be a considerably higher rental and royalty rate under the Class II reinstatement requirements. Reinstatement procedures are provided in Manual Section 3108 and Handbook 3108-1. If lease termination occurs, pending reinstatement of the lease, further lease development shall not be authorized, and production revenues, if any have been obtained, must be placed into an escrow account in their entirety (not just the potential royalty amount), since any drilling and production after the termination of the lease is unauthorized until reinstatement of the lease is approved.

RENTAL PAYMENT
REQUIRED FOR
DRILLING OVER
PRIMARY
LEASE TERM

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H. Adjudicative Processing - Drilling Extension

Responsible Official	Step	Action	Keywords
APD Approving Officer	1.	Notify SO lease adjudication whenever it is anticipated that drilling may be in progress over the end of the primary term of a lease. Notification to SO lease adjudication by a copy of the APD face sheet, either before or after approval of the APD, or by some other method, will ensure that the lease case is processed properly and not treated as a routine expiration.	NOTIFICATION OF POSSIBLE EXTENSION
	2.	Make the determinations necessary for leases on or for which drilling operations were progressing as soon as possible after the expiration date of a lease, following the guidance provided in the Sections I.B through I.G, above.	
	3.	Send the appropriate report to SO lease adjudication (see Illustrations 1, 2, and 3).	
	4.	If a determination is made that the operations were not diligent, see Step I.I.3, in the next section of this Handbook.	
Adjudication	5.	Receive evidence of payment of the 6th or 11th year rental from the Minerals Management Service (MMS), or other evidence that lease may be extended due to diligent drilling over the expiration date.	
Docket	7.	Charge lease case file to Adjudication.	
Adjudication	8.	Determine if sufficient rental is received and if there is any indication that the lease is eligible for an extension. If no notification from FO operations personnel has been received, request a report on diligent drilling performed on the lease or in the communitized area or unit to which the lease is committed.	VERIFICATION OF POSSIBLE EXTENSION

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Responsible Official	Step	Action	Keywords
Field Office Operations	9.	Report to SO lease adjudication any drilling operations diligently performed that allow lease to be extended. If drilling activities do not warrant lease extension, see Step I.I.1, in the next section of this Handbook.	DILIGENCE REPORT - EXTENSION GRANTED
Docket	10.	Charge lease case file to Adjudication.	
Adjudication	11.	Issue decision to lessee extending term of lease for 2 years.	DECISION EXTENDING LEASE TERM
	11a.	<u>EXAMPLE</u> : For a lease expiring May 31, 1994, the 2-year extension period begins June 1, 1994, and ends at midnight May 31, 1996 (see Illustration 4).	
	12.	Transmit copy of decision to MMS, Data Management Division (DMD), to indicate new lease expiration date.	
	12a.	If for any reason, the lease has been removed from the MMS-DMD automated system, prepare an accounting advice to reactivate the lease in the Common Reference Database (see Illustration 5).	
ALMRS Entry	13.	Update Case Recordation as follows:	AUTOMATED NOTATION
	13a.	Enter Action Date (MANDATORY ACTION CODE): Date of decision extending lease; DE 1775 Action Code 258/DE 2910 Action Code 235; Action Remarks: THRU MM/DD/YY; DIL DRLG; and	
	13b.	Enter Action Date (MANDATORY ACTION CODE): Date extended lease expires; DE 1775/2910 Action Code 763.	

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I. Adjudicative Processing - Determination of No Diligence

Responsible Official	Step	Action	Keywords
Adjudication	1.	Receive report from FO operations that lease operations are not diligently pursued or report of other noncompliance (see <u>Daisy Hook, et al.</u> , 21 IBLA 147 (1975) and Illustration 3).	NONDILIGENCE REPORT/ EXTENSION DENIED
Docket	2.	Charge lease case file to Adjudication.	
Adjudication	3.	Issue decision to lessee holding that lease expired with 30-day right of appeal (see Illustration 6).	
ALMRS Entry	4.	Update Case Recordation (if not already indicated through the BLM/MMS Automated Data Transfer process):	AUTOMATED NOTATION
	4a.	Enter Action Date (MANDATORY ACTION CODE): Date lease expired; DE 1775 Action Code 762/DE 2910 Action Code 234; Action Remarks: NO DIL DRLG.	
Adjudication	5.	After 30-day appeal period has expired, prepare accounting advice to authorize refund of rental by the MMS-DMD (see Illustration 7). If an appeal is filed, see Handbook 3100-1, Chapter 1.	RENTAL REFUND
ALMRS Entry	6.	Enter Action Date: Date refund authorized for 6th/11th year rental; DE 1775 Action Code 092/DE 2910 Action Code 379; Action Remarks: Amount; 6TH/11TH RENT.	AUTOMATED NOTATION
Adjudication	7.	Route case file for records update and competitive processing.	

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